

Message Text

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ACTION EB-04

INFO OCT-01 SS-04 ISO-00 EUR-03 TRSE-00 CEA-01 NSC-04

NSCE-00 INR-01 INRE-00 CIAE-00 FRB-01 SSO-00 /019 W

----- 118458

O R 261229Z APR 76

FM AMEMBASSY LONDON

TO SECSTATE WASHDC IMMEDIATE 1077

INFO TREASURY DEPT WASHDC IMMEDIATE

AMEMBASSY BONN

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY TOKYO

USMISSION OECD PARIS

C O N F I D E N T I A L SECTION 01 OF 02 LONDON 06300

LIMDIS GREENBACK

DEPARTMENT PASS FRB

TREASURY PASS LISLE WIDMAN AND DONALD SYVRUD, OASIA

E.O. 11652: GDS

TAGS: EFIN, UK

SUBJECT: STERLING

REF: LONDON 6247

1. DESPITE AN INCREASE IN THE MINIMUM LENDING RATE OF 150 BASIS POINTS LAST FRIDAY, TO 10-1/2 PERCENT STERLING REMAINS UNSETTLED AND VOLATILE THIS MORNING WITH NO UNDERLYING SUPPORT. LAST FRIDAY'S TREASURY BILL AUCTION RATE ROSE BY 1.5548 PERCENT TO 9.9872 PERCENT, RESULTING UNDER THE FORMULA IN AN INCREASE IN THE MLR TO 10-1/2 PERCENT. THE 500 MILLION POUNDS IN BILLS OFFERED AND ALLOTTED ATTRACTED BIDS OF 806.8 MILLION POUNDS (THIS WEEK, 550 MILLION POUNDS WILL BE ON OFFER REPLACING MATURITIES OF 400 MILLION POUNDS).

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2. THIS MORNING DEALERS IN MAJOR COMMERCIAL BANKS AND AT THE BANK OF ENGLAND NOTE THAT AFTER STERLING'S CLOSE OF \$1.8230 IN LONDON ON FRIDAY. STERLING HAD CONTINUED TO FALL IN NEW YORK ON FRIDAY AFTERNOON. CLOSING AT 180.70. DEALERS HERE ARE NOT SURPRISED. BECAUSE UNDERLYING SUPPORT FOR THE POUND WAS NOT SEEN IN NEW YORK AND ON A FRIDAY AFTERNOON WITH NEW YORK BEING THE LAST MAJOR MARKET OPEN, AN UPTURN WOULD NOT HAVE BEEN EXPECTED.

3. THIS MORNING IN LONDON A NEW RECORD LOW FOR THIS MARKET WAS SET WHEN STERLING HIT \$1.8070 AND THE TRADE WEIGHTED DEVALUATION WIDENED TO 38.2. AT NOON LONDON TIME STERLING WAS AT \$1.8125, THE TRADE-WEIGHTED DEPRECIATION AT 38.0. THE MARKET IS CONSIDERED AS MUCH LESS VIOLENT THAN ON THURSDAY AND FRIDAY AND SUSPICIOUSLY QUIET, TURN-OVER SMALL. THERE HAS BEEN NO POSITIVE REACTION AS A RESULT OF THE MLR INCREASE. DEALERS REPORT THAT THE CONTINUING PRESSURE ON STERLING IS NOT FROM SPECULATION. BUT RATHER FROM EXISTING HOLDERS, PARTICULARLY SMALL HOLDERS SELLING OUT.

4. ON A CONFIDENTIAL BASIS. THE BANK OF ENGLAND REPORTS THAT WHEN IT DOES INTERVENE TO TAKE A PERSONAL SALE, SAY 250 THOUSAND POUNDS, IN ORDER TO PROVIDE SUPPORT. IT FINDS THAT TWO OR THREE OTHER SELLERS COME IN AT THE SAME RATE AS WELL. SALES THUS FAR SEEN BY THE MARKET ARE NOT CONSIDERED TO BE BY MAJOR STERLING HOLDERS BUT RATHER BY SMALLER SELLERS WHO APPEAR TO BE GETTING OUT ON THE UPTICK IE, WHEN THE RATE RISES. THE RATE TENDS TO DRIFT DOWN WHETHER OR NOT THE BANK OF ENGLAND ATTEMPTS TO PROVIDE SUPPORT.

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FM AMEMBASSY LONDON
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C O N F I D E N T I A L SECTION 02 OF 02 LONDON 06300

LIMDIS

5. ONE OF THE PSYCHOLOGICAL FEARS HEARD HERE THIS MORNING IS THE POSSIBILITY THAT MAJOR OPEC HOLDERS SUCH AS KUWAIT, ABU DHABI AND DUBAI THAT HAVE GILT EDGED AND OTHER INVESTMENTS MATURING IN COMING WEEKS MAY DECIDE TO SHIFT INTO DOLLARS, DM AND SWISS FRANCS, IN EFFECT CUTTING THEIR LOSSES ON THE EXCHANGE RATE. ANOTHER, IN PART RELATED, IS THAT IF STERLING DROPS BELOW \$1.80, IT MAY HAVE BREACHED ANOTHER PSYCHOLOGICAL SUPPORT LEVEL, WITH FURTHER SHARP FALLS POSSIBLE. IN ATTEMPTING TO ASSESS BASIC TRENDS AND FUTURE OUTLOOK. DEALERS SUMMARIZE SITUATION BY SAYING THERE IS NO UNDERLYING SUPPORT, NO ONE WANTS TO HOLD STERLING AND THOSE WHO HAVE IT WANT TO GET OUT. THERE IS SOME FEAR OF TIGHTER SHORT-TERM INTEREST RATES IN THE U.S. WHICH COULD STRENGTHEN THE DOLLAR. WHEREAS ON AN ECONOMIC BASIS, PERHAPS IT IS RIGHT TO CONCLUDE THAT THE STERLING RATE IS ROUGHLY WHERE IT SHOULD BE, THE PSYCHOLOGICAL FACTORS ARE STILL DEPRESSING. THESE INCLUDE FEARS THAT EVEN IF AN AGREEMENT ON A SECOND STAGE OF INCOMES POLICY IS REACHED QUICKLY WITH THE TUC. THAT IT
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WILL NOT HOLD. THERE WAS A 3-HOUR MEETING ON FRIDAY EVENING, HEADED BY CHANCELLOR HEALEY FOR THE GOVERNMENT AND TUC GENERAL SECRETARY LEN MURRAY, AIMED AT SPEEDING UP A DECISION ON SECOND STAGE OF INCOMES POLICY AND AN EXHORTATION ON SUNDAY FROM THE PRIME MINISTER TO TRADE UNIONISTS TO SUPPORT THE GOVERNMENT'S PROPOSALS ON THE BASIS OF THEIR OWN SELF INTEREST: DESPITE THE EXHORTATIONS THE MARKET IS NOT IMPRESSED, IN LARGE PART BECAUSE OF CONTINUED TUC OPPOSITION TO THE 3 PERCENT PLAN AND THE UNCERTAINTY OF THE EVENTUAL OUTCOME. IN ADDITION. WILDCAT STRIKES SUCH AS THOSE BEING EXPERIENCED AT LEYLAND ARE CITED. SINCE MARCH 4. STERLING'S DOWNWARD SLIDE HAS PRODUCED A VOTE OF NO CONFIDENCE FROM THE MARKET.

ARMSTRONG

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